

March/April 2003

CALIFORNIA FRANCHISE TAX BOARD

Tax News

Major changes in FTB guidelines for obtaining good standing letters

Upon request, we will issue a document stating whether or not a business entity is in good standing with us. Effective this year, we've made significant changes to the guidelines for obtaining that information from us.

Document name change

Since the purpose of the document is to disclose in writing a business's current status with us, we've changed its name from *Letter of Good Standing* to *Entity Status Letter*. The information in the letter is public and does not

reflect the entity's status with any other agency (e.g. the California Secretary of State).

Fees

Effective January 2003, we generally increased the charge for the requestor of an Entity Status Letter to \$20 per letter for corporations and limited liability companies taxed as corporations. Effective February 1, 2003, we have instituted a charge of \$20 for each exempt organization entity status letter.

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New real estate withholding law in effect

Assembly Bill 2065, which requires buyers of California real estate to withhold 3 1/3 percent of the total sales price, took effect January 1, 2003.

This new law expands tax withholding to all individuals who sell California real property, including California resident individuals.

There are some exceptions in the law. Withholding is not required if the total sales price is \$100,000 or less, the property is the seller's principal residence, the sale results in a taxable loss, the transaction qualifies as a like kind exchange, and some involuntary conversions.

Also exempted are sales where the seller is a tax-exempt entity, a California corporation, or partnership.

Real estate withholding is a prepayment of state income taxes for sellers of California real estate. In many cases, withholding saves the seller from having to make estimate payments to cover the tax due on the gain on the real estate sale.

How to get AB 2065 information

Various efforts have been undertaken to communicate this new law to withholding agents and the public. Our staff has already conducted over 50 presentations around the state, and we're doing more. Escrow companies or associations interested in our AB 2065 presentation should send requests to WSCS.seminar@ftb.ca.gov or visit our Website at www.ftb.ca.gov.

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Tax News

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TAX NEWS is a bimonthly publication of the Communications Services Bureau, California Franchise Tax Board. Its primary objective is to provide information to income tax practitioners about state income tax laws, regulations, policies and procedures.

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For information about a client's account, contact:

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fax: (916)845-6377

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FTB on the Internet
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New AB 2065 forms available

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We've updated our Withholding Services and Compliance Section's Interactive Voice Response phone system to provide more specific options to customers when trying to access information or forms. The toll free number is (888)792-4900.

Forms

The new forms (for escrows closing on or after January 1, 2003), along with the updated FTB Publication 1016, *Real Estate Withholding Guidelines*, are available from our Website. The new forms include:

- Form 597 - Real Estate Withholding Tax Statement (fillable).

- Form 593-C&L - Real Estate Withholding Booklet for Individuals.
- Form 593-W - Real Estate Withholding Booklet for Non-Individuals.

Forms related to the Entertainment Withholding Program, Withholding by Partnerships and LLCs on Nonresident Partners and Members, Independent Contractors and Rents & Royalties Withholding are still included in the Package X.

For more information about the new real estate withholding requirements, visit www.ftb.ca.gov or call toll free 1-888-792-4900.

Important change to Form FTB 541 Booklet

Please note the following change to the distributed 2002 Form FTB 541, *Fiduciary Income Tax Booklet*. Should you have any questions about this change, contact our Tax Forms Development and Distribution Section at (916) 845-3442.

Form FTB 541, *Fiduciary Income Tax Booklet*

This change appears on page 11 of the instructions, under the heading *Other Information*. It reads:

Line 5 - Enter the fair market value of all of the assets held by the trust at the close of the trust's taxable year. An independent appraisal of the trust's assets is not required.

For cash, cash equivalents, and publicly traded securities, provide the value contained on the trust's most current bank, brokerage, or other independently prepared financial statement. For real

and tangible personal property, intangible property, securities for which there is no readily ascertainable fair market value, and interests in entities other than corporations (i.e. partnerships, LLCs, other trusts, etc.), provide a good faith estimate of the property's value.

If the trust did not hold any assets at the end of its taxable year, enter the fair market value of the trust's assets at the beginning of the taxable year and write "beginning" in the margin next to this question.

The Internet version is updated. You can view, download, and print this and other California tax forms and publications from our Website at www.ftb.ca.gov.

For the most current information about changes to our tax forms and publications, go to *Tax News Online*, located in the *Tax Professionals Portal* of our Website. The address is: www.ftb.ca.gov/professionals.

Major changes in FTB guidelines for obtaining good standing letters

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The fee more accurately reflects our cost to process these requests.

We **do not** charge a fee for the following:

- Requests made within 30 days of an account's good standing restoration date
- Requests made for limited liability companies taxed as partnerships or as disregarded entities (e.g., single-member limited liability companies).

Eligibility guidelines

We will issue Entity Status Letters for:

- Corporations.
- Exempt organizations.
- Limited liability companies taxed as corporations, partnerships, or disregarded entities (e.g., single-member limited liability companies).

We **do not** issue entity status letters for:

- General partnerships.
- Limited partnerships.
- Limited liability partnerships.

However, any of these entities registered with the Secretary of State can send a written request for a

Certificate of Good standing to:

Secretary of State
(Limited Partnership, Limited Liability Partnership, or General Partnership) Section
PO Box 944225
Sacramento CA 94244-2250

Where to get entity status letters

You can request status letters at the public counter of any of our field offices. Sacramento area legal services couriers with bulk requests must submit them via email to GSL@ftb.ca.gov. You can also make requests through the mail.

For eligible entities other than exempt organizations, please send your request to:

Franchise Tax Board
PO Box 942857
Sacramento CA 94257-0501

For exempt organizations, please send your request to:

Exempt Organizations Unit MS D-16
PO Box 1286
Rancho Cordova CA 95741-1286

If you have any questions about obtaining an entity status letter, contact the Tax Practitioner Hotline at (916) 845-7057.

Attention substitute, scannable forms users:

If you're using substitute and scannable California income tax forms, be sure that the forms generated by your software program meet our requirements for substitute forms.

To learn how, visit *Tax News Online*

and read the article entitled:

Tax forms and publications update:
Are your 2002 substitute, scannable forms FTB approved? There you'll find a list of tax preparation software companies that have agreed to comply with our tax forms requirements for the 2002 tax year.

Ask the Advocate



Debbie Newcomb
Taxpayer
Advocate

Q: Do my clients need to send their property tax bills along with their applications for homeowners assistance?

A: Yes. Here's why: Last year the Governor signed into law Senate Bill 1875 (Karnette). This bill allows the Franchise Tax Board to clarify requirements for the Homeowners and Renters Assistance Program, making it easier for claimants to apply for and receive assistance payments. Senate Bill 1875 eliminated the requirement that homeowner filers attach their annual property tax statement to their filed claim; instead authorizing FTB to prescribe the information necessary to constitute a valid claim.

We are currently drafting regulations to implement this legislation. We will address any proposed procedural changes that affect claimants as part of the regulation adoption process. We are also researching new methods for processing claim forms and for gathering the information we need to validate claims. For now, however, the procedures for filing a claim are unchanged. Delays in processing homeowner claims and

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“We’re closing the business”

Avoid these costly mistakes when dissolving clients’ corporations

Making the decision to end a business can be difficult. But once a client makes that decision, there are some things you can do to ensure that officially ending the business in California is completed smoothly and efficiently.

First, make them aware that simply checking the final return box on their next tax return will not officially dissolve their corporation. Next, carefully follow the Secretary of State’s, www.ss.ca.gov/business/corp/corp_stkdissinfo.htm, prescribed procedures for the proper dissolution of a corporation (located in the California Corporations Code).

Pay particular attention to the timing of the filing, and make sure all documents are filled out completely and signed by the appropriate parties so the Secretary of State can accept them the first time you submit them. Otherwise, under the current laws (California Revenue and Taxation Code Section 23151) your client may be required to file another tax return, and pay additional taxes, penalties, and interest. The date the Secretary of State receives a complete and qualified application will be the conditional date of dissolution. For example:

Corporation A, filing on an annual basis, submits a letter on Dec. 15, 2002, to the Secretary of State requesting a dissolution. None of the required forms are submitted (as outlined in the California Corporations Code). Upon review, the Secretary of State determines that the documents are incomplete and informs the corporation that it must submit specific forms (Certificate of Dissolution, statement of officer(s), etc.).

Corporation A delays in submitting the forms and as a result, they do not reach the Secretary of State until Feb. 5, 2003.

The Secretary of State accepts the submitted forms and completes the filing of *Corporation A*’s dissolution. The Secretary of State informs us that the *conditional dissolution date* is actually Feb. 5, 2003, not Dec. 31, 2002, as *Corporation A* had planned.

Corporation A will be required to file an additional tax return, even though it did not conduct business or earn income for the short period ending Feb. 5, 2003. *Corporation A* must pay at least the minimum tax (we would also assess penalties and interest for a late return, if applicable). The key to this example is submitting correct forms and establishing the *conditional date of dissolution*.

Conditional date of dissolution

A corporation continues to exist until the Secretary of State establishes its *conditional date of dissolution*. This date also serves as the end of the corporation’s final tax year. For example: *Corporation B* wants to dissolve. It has a filing period of Jan. 1, 2003 to Dec. 31, 2003. The corporation files accepted dissolution forms with the Secretary of State dated June 30, 2003. Its final tax year-end will be June 30, 2003. Its final tax return will be due *two months and fifteen days* from the date of conditional dissolution as established by the Secretary of State (Sept. 15, 2003). Even if the corporation did not conduct business, or operated at a loss, it is still subject to filing requirements with a tax year-end of June 30, 2003 (as established by the Secretary of State).

Tax Clearance Certificate

A dissolving corporation must submit a completed Form FTB 3555, *Request for Tax Clearance Certificate* - *Corporations* (except as provided by California Corporations Code Section 1900.5).

Corporations can submit the FTB 3555 to the Secretary of State with all the other required forms. The Secretary of State will forward it to us for completion. At this point, the corporation’s dissolution will be considered *conditional* pending our issuance of the *Tax Clearance Certificate*.

Once we verify that the corporation has filed all due tax returns and paid any taxes due at the time of application, we’ll notify the Secretary of State and issue the *Tax Clearance Certificate*. The dissolution will become *final* as of the date the corporation initially filed its *Certificate of Dissolution* with the Secretary of State.

When filing the corporation’s final tax return, be sure to complete the section indicating that it is final by filling in the correct status and the applicable date. Remember, this information is based on the status and date as filed with the Secretary of State. Often we receive tax returns containing the incorrect

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Ask the Advocate

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in issuing assistance payments will occur if the property tax bill is not included with the claim form.

You can always obtain detailed information about the program by visiting our *Homeowners and Renters Assistance Program* Webpage at www.ftb.ca.gov/individuals/hra/index.html.

“We’re closing the business”

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information (e.g. the date that the corporation ceased doing business, the end of their tax year, or the date they completed a merger).

A corporation is considered active, and thereby subject to filing and tax requirements, until it prepares and submits its *Certificate of Dissolution* with the Secretary of State.

Consequently, when we process a tax return with a *final return* indicator, we review the account to determine if the corporation submitted a *Certificate of Dissolution* with the Secretary of State. If it hasn’t, we send the corporation a notice and instructions.

We issue a tax clearance when the corporation files a form FTB 3555, *Request for Tax Clearance Certificate-Corporations*. You can download form FTB 3555 from our Forms and Publications page. Send the completed form FTB 3555 to the Secretary of State along with the documents required to dissolve. The address for the Secretary of State’s office is on form FTB 3555. You can get information regarding the required documents from the Secretary of State’s website at www.ss.ca.gov or call (916) 657-5448.

A corporation can obtain a *Tax Clearance Certificate* using one of these four methods:

1. Furnish an assumer - either an individual, corporate, trust, Limited Liability Company or Limited Liability Partnership
2. Post a cash deposit (minimum amount \$2,000)
3. Post a surety bond (minimum amount \$2,000)
4. Request a tax clearance certification on the basis that taxes are paid (filing of all required returns and payment of all required taxes)

Assumer basis or taxes paid basis

If the corporation is dissolving using *taxes paid* basis, it must file all tax returns and pay all taxes prior to receiving a *Tax Clearance Certificate*. Corporations choosing this method should ensure that the final return is filed as soon as they receive verification from the Secretary of State that their forms have been accepted. We will not issue a tax clearance until we receive the final return.

If the corporation is dissolving on an *assumer* basis, it must certify that an individual, corporation or other qualified entity will assume responsibility for filing a final return and paying any future taxes due.

Corporations that dissolve on the *assumer* basis may be subject to filing requirements after they receive their *Tax Clearance Certificate*. The reason is due to timing differences. A final return may not yet be due when the *Tax Clearance Certificate* is issued.

For example, *Corporation B* has a January 31 tax year-end. It submitted its dissolution documents to the Secretary of State on December 1, and received its *Tax Clearance Certificate* the following January. *Corporation B*’s final return is due *two months and fifteen days from the date of conditional dissolution as established by the Secretary of State (due date is February 15)*.

The *Tax Clearance Certificate* was issued when *Corporation B* met all our requirements for formal dissolution. The tax return would be filed for the period ending on the date of the *conditional dissolution*. Section 23334 of the Revenue and Taxation Code states in part that:

The issuance of a certificate shall not

relieve the taxpayer or any individual or corporation from liability for any taxes, penalties, or interest imposed...

All corporations must file a tax return through their final tax year-end (including short periods) and pay at least the minimum tax. We include a reminder to file on the *Tax Clearance Certificate*. Corporations/assumers may receive a statutory assessment if they fail to file the final return. *Note: All tax returns remain subject to audit through normal statutory periods.*

Foreign or domestic corporation?

The above explanation applies to *dissolving domestic* stock corporations only. Foreign qualified corporations cannot dissolve in California and do not receive a conditional dissolution. They can only surrender, withdraw or merge in California. For foreign corporations, the requirement to file returns and pay taxes continues through the date of termination in California.

Three-member Board has new members

Steve Westly is the state’s new Controller and now serves as chair of the three-member California Franchise Tax Board.

Carole Migden, the new chair of the State Board of Equalization is the second new member of the three member board.

Steve Peace is the new Director of the Department of Finance and is the board’s third new member.

Proposed legislation

The California Legislature has returned to business for the 2002 – 2003 legislative session, introducing several income tax bills intended to resolve the budget crisis, stimulate the economy, or assist taxpayers. This is just a partial listing of the proposed legislation that was available for publication at press time. For more details and analyses of these and other bills, visit our Legislative Information Webpage located on the Web at www.ftb.ca.gov/law_legis/index.html.

Personal income tax rates

AB 4 (Assemblymembers Wilma Chan and John Dutra) is an *intent* bill, expressing the Legislature's intention to increase the tax rates on high-income taxpayers. AB 4 does not currently specify what the percentage increase would be, only that it would apply to individuals with taxable income over \$130,000, an amount doubled for married taxpayers.

SB 4 (Senator Dennis Hollingsworth) would gradually reduce all personal income tax rates, decreasing them to zero by 2007, and also eliminate the alternative minimum tax in 2007. SB 4 also would change the imposition and calculation of tax for part-year taxpayers and nonresidents.

AB 82 (Assemblymember Robert Dutton) would increase the renter's credit from \$60 to \$185, and from \$120 to \$370 for married couples, heads of household, or surviving spouses. AB 82 would eliminate the income limits, so that every renter could claim the credit, and adjust the credit amount annually for inflation.

AB 82 also would increase the homeowner's property tax exemption from \$7,000 to \$32,000 and require the Board of Equalization to adjust the amount annually for inflation.

Voluntary contributions

AB 132 (Assemblymember Edward Chavez)

AB 137 (Assemblymembers Edward Chavez, Lou Correa, Mervin Dymally, and Sally Lieber)

These bills would change the repeal date for the *California Fund for Senior Citizens*, which supports the California Senior Legislature and its activities on behalf of older persons. AB 132 would extend it from January 1, 2005, to January 1, 2010, while AB 137 would eliminate it, keeping the fund on the tax returns forever.

SB 43 (Senator Gilbert Cedillo) would extend the repeal date for contributions to the Department of Social Services to support the Emergency Food Assistance Program from January 1, 2004, to January 1, 2009.

Enterprise zones

AB 11 (Assemblymembers Bonnie Garcia and Juan Vargas) would require the Technology, Trade, and Commerce Agency to designate the city of Brawley as an enterprise zone. This designation would allow businesses in Brawley to claim special income tax benefits.

Manufacturers' Investment Credit

The existing Manufacturers' Investment Credit specifies that it will be repealed on January 1, 2001, or on January 1 of any year that total employment in California does not exceed by 100,000 jobs the total employment on January 1, 1994. Concerns that the 100,000-job threshold will not be met have led to three bills that will ensure the credit's continued operation.

AB 122 (Assemblymember Ronald Calderon) would extend the repeal date from January 1, 2001, to January 1, 2006.

SB 47 (Senator Dick Ackerman and Charles Poochigian) and **SB 2X (Senators Dick Ackerman and Charles Poochigian)** would both delete the repeal date and the threshold test, making the credit available forever.

Irrigation system improvement

AB 63 (Assemblymembers Dave Cogdill and Bonnie Garcia) This bill would establish a credit for purchasing and installing an *irrigation system improvement*. The term *irrigation system improvement* is broadly defined, but is generally intended to improve water usage in farming. The improvement would have to be installed in California and certified by a professional. The credit amount would be 25 percent of the taxpayer's costs, up to a limit of \$150 per acre, and the credit would be available between 2003 and 2008.

California Internet Tax Freedom Act

AB 128 (Assemblymember John Campbell) would extend the repeal date for the *California Internet Tax Freedom Act*, which generally prohibits cities or counties from imposing taxes on Internet activities to January 1, 2008. The current law will expire on January 1, 2004. AB 128 would eliminate the current language establishing a connection between the *Freedom Act's* repeal date and the requirement that the *California Commission on Tax Policy in the New Economy* prepare an interim report on California's economy.

General Fund related spending limits

ACA 6 (Assemblymember John Campbell) would replace the existing provision in the Constitution on spending limits with new language. Expenditures from the State's General

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Use e-file to schedule clients' estimate payments

When you e-file your clients' 2002 tax returns, you can conveniently schedule electronic funds withdrawal requests for any or all of their 2003 estimated tax payments. Your software will prompt you to specify the withdrawal date and the amount of the estimated

tax payments and will display the information on your client's form FTB 8453, *California e-file Return Authorization*.

To cancel any electronic funds withdrawal payment, your client must call our e-file Help Desk at

(916) 845-0353 at least two business days before the date of the withdrawal.

Check with your software provider to find out if the electronic funds withdrawal feature for estimated tax payments is offered.

Important e-file information now available on CD-ROM

For the first time, we've included everything you need for a successful e-filing season on a CD-ROM.

In the past, we provided e-file information to you using paper publications and documents. The CD-ROM contains:

- Our Franchise Tax Board e-file guidelines.
- Information about new legislation impacting e-file.

- New forms.
- Access to ordering e-file marketing supplies, such as notepads and magnets.
- The info you need to print your own e-file stickers.

We mailed the CD-ROM to approved e-file providers in late December. If you are an approved e-file provider and you didn't receive a CD-ROM from us, please call the e-file Help Desk at (916)

845-0353 to request one. You can email your request to e-file@ftb.ca.gov.

If you are not in our e-file program yet, you can download our e-file program enrollment form (Form FTB 8633) from our website at www.ftb.ca.gov/forms/02_forms/02_8633.pdf. You can fax your completed, signed enrollment form directly to us. Once you are accepted into the e-file program, we'll mail a CD-ROM to you.

It's not too late to file paperless K-1s for 2001 tax year

Depending on your clients' fiscal year, it may not be too late to file paperless Schedules K-1 (565 or 568) for the 2001 tax year. Also, if you will be amending your client's 2001 Tax Year Schedules K-1 (565 or 568), you can use the Paperless K-1 Program to file.

Using our Paperless K-1 Program means a reduction in paperwork, printing and postal costs for you.

For more information, please visit: www.ftb.ca.gov/businesses/eServices/k1.

And don't forget to visit our all new Website for e-file professionals at www.ftb.ca.gov/professionals/eservices/.

Proposed legislation

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Fund and special funds could increase annually only by the cost of living. This limit may be exceeded for an emergency, such as a military attack or natural disaster. However, the increased spending caused by the emergency would not become part of the expenditure calculation for next year.

If any services are transferred from the state government to the local government, then the expenditure level would be reduced by the cost of those services. Also, if the Legislature or a state agency imposes a new program or higher level of service on a local government, then the state is generally

required to provide more money to the local government.

Any revenue over the expenditure limitation would be allocated to a *Special Reserve Account*, to the educational system, or rebated to taxpayers, depending on specified conditions.

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